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# Further Scrutiny of College and University Endowments

HIGHER EDUCATION, NOT-FOR-PROFIT, TAX
BY SCHNEIDER DOWNS PROFESSIONAL

On September 13, 2016, the House Ways and Means Subcommittee on Oversight held the first of several anticipated hearings to address the manner in which the tax code affects higher education. The hearing, entitled "Back to School: Review of Tax-Exempt College and University Endowments," spotlighted endowments and covered several related issues, including student debt, spending transparency, and endowment and institutional spending on non-educational uses, such as athletic costs, campus amenities and administrative costs.

## **Background**

Congressional interest in college and university endowments is not new. In January 2008, the Senate Finance Committee sent a letter to 136 colleges and universities that had endowments of $500 million or more. The inquiry focused on endowment management and how the institutions were making college education more affordable for low- and middle-income families. The letter asked for information concerning the institution's tuition costs and financial assistance packages.

In addition, in 2008, the Internal Revenue Service sent a questionnaire to 400 colleges and universities. The questionnaire sought information on each institution's endowment and made inquiries concerning executive compensation and unrelated business income. With the onset of the 2008 financial crisis, however, Congressional scrutiny regarding college and university endowments appeared to fade.

*Renewed Interest*

In October of 2015, the House Ways and Means Subcommittee on Oversight ("Subcommittee") held a hearing to discuss the rising costs of a college education and related tax policy. The stated purpose of the hearing was to examine federal tax policies affecting colleges and universities and whether federal tax policies were partly the reason for the increase in costs. The hearing focused on endowment spending and tuition increases, compensation paid to top administrators and coaches, and the growth of institutional administrative costs. During the discussions, the Subcommittee inquired as to whether institutions of higher education made sufficient use of their endowments and investment earnings for student aid.

*Report from the Congressional Research Service*

In December of 2015, the Congressional Research Service ("CRS") published a report addressing possible changes to the federal income tax treatment of college and university endowments and how changes could further various tax policy objectives.

CRS is a nonpartisan research entity that provides reports to Congress and Congressional committees upon request.

The CRS report, entitled “College and University Endowments: Overview and Tax Policy Options,” provided comprehensive data concerning college and university endowments. For example, the CRS report stated that, in 2014, 11% of the tax-exempt institutions of higher education held 74% of all endowment assets.  CRS also determined that if the endowment income from colleges and universities was taxed at the highest corporate tax rate of 35%, the estimated revenue generated for FY 2014 would have been $16.2 billion.

CRS addressed four specific tax reform options in the report with respect to college and university endowments:

- Imposition of a payout requirement similar to the distribution requirement currently imposed on private foundations;
- Imposition of a tax on endowments or endowment earnings;
- Limitation on charitable deductions for gifts to endowments; and
- Changing the current taxation policies with respect to certain offshore investments.

CRS observed that the current favorable tax treatment provided to college and university endowments could be changed to encourage additional spending from endowments towards specific purposes, such as tuition assistance. However, CRS made no specific recommendations.

*Joint Congressional Inquiry*

On February 8, 2016, the Senate Committee on Finance and the House Ways and Means Committee sent a joint letter to 56 colleges and universities with endowments greater than $1 billion requesting information on each institution’s endowment.  The letter requested information about how the institution was using its endowment to fulfill its charitable and educational purpose.  Specifically, the inquiry asked for information from the past three tax years regarding the following:  endowment management; endowment spending and use of funds; donations and information concerning naming rights given in connection with donations; and policies and vetting processes used to identify conflicts of interest with respect to endowment investments.   Some of the responses to the joint inquiry are posted on the internet.

## The Latest Congressional Hearing

At last month’s Congressional hearing, five witnesses were invited to speak:

- *Neal McCluskey, Director of the Center for Educational Freedom of the Cato Institute ,*
- *Jeff Amburgey, Vice President for Finance for Berea College,*
- Sheila Bair, President of Washington College (former chair of the Federal Deposit Insurance Corporation),
- *Mark Schneider, Vice President and Institute Fellow of the American Institutes for Research (former Commissioner of the National Center for Education Statistics),* and

- *Sandy Baum, PhD, Senior Fellow at the Income and Benefits Policy Center of the Urban Institute .*

In discussing a number of issues related to the college affordability problem, the speakers identified a number of possible solutions. However, several speakers noted that using endowments alone as a funding source is not necessarily the solution to curbing the rising cost of education for many reasons, including donor restrictions, instability of return on endowment investments, and the fact that only a small number of colleges and universities have endowments over $500 million. In addressing affordability, the Subcommittee also indicated that it was very interested in achieving greater transparency from institutions of higher education with respect to expenditures, questioning whether the Form 990 could be revised to differentiate between expenses that are educational as opposed to those that are not.

The rationalization for the investigative hearings is that Congress wants to better understand the public benefit of the tax breaks provided to tax-exempt colleges and universities, as well as tax breaks given to donors who receive a tax deduction for charitable contributions made to colleges and universities. Accordingly, it is anticipated that intense Congressional scrutiny of the tax-exempt higher education sector, including tuition increases, spending habits and use of endowment funds, is likely to continue.

Additional information concerning the hearing can be found at http://waysandmeans.house.gov/event/hearing-tax-exempt-college-university-endowments.

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